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February 10, 2003

TO: Each Supervisor

FROM: Thomas L. Garthwaite, M.D.
Director and Chief Medical Officer

SUBJECT: **BUDGET COMMITTEE OF THE WHOLE – FEBRUARY 11, 2003**

This is to provide your Board with an update on the status of the County's discussions with the State and Federal governments on the County's health crisis and provide an update on the Department's fiscal outlook.

Federal / State / County Discussions Update

On February 7, the Centers for Medicare and Medicaid Services (CMS) and the State of California reached agreement on the renewal of the State's Selective Provider Contracting Program (SPCP) waiver.

The agreement contained specific benefits for Los Angeles County's health system including:

- A one-time \$50 million payment directed to Los Angeles County under the terms of the settlement of the Orthopaedic Hospital lawsuit related to outpatient Medi-Cal rates (subject to court approval)
- An additional \$50 million in supplemental Medi-Cal inpatient payments in both Fiscal Years 2002-03 and 2003-04.
- The State of California also announced that it will allocate an additional \$100 million in funding over two years to Los Angeles County from SPCP funds.

This makes the total direct benefit to Los Angeles County \$250 million under the extension and transition agreement.

Additional Sources of Funding from Federal and State Sources

Under the extension agreement and transition document, there is also a State and Federal commitment to pursue flexibility and reform in the Disproportionate Share Hospital (DSH) funding program for Los Angeles County to support outpatient care and related system reforms.

Separately, and pursuant to Governor Davis' November plan to assist safety net systems throughout the State, the State and County are working on a number of other funding sources to stabilize Los Angeles County's health system beyond the two years under the SPCP Waiver. In addition to the County's DSH flexibility proposal, these sources of funding include increasing Medi-Cal rates to government operated Medi-Cal managed care programs and the pursuit of federal Medicaid matching funds for a portion of voter-approved Measure B that may be used to provide supplemental Medi-Cal payments for trauma centers.

These additional sources of support for the County health system are vital and DHS plans to pursue them aggressively.

CMS also included in the transition agreement a goal for Los Angeles County to increase DHS inpatient hospital discharges with Medicare and commercial payer sources by 6 percent. The State is to present a work plan to CMS within 90 days outlining the plan to achieve this goal. As this is a goal and not a requirement, CMS and the State have made clear that there is not a penalty should the County be unable to realize it. Also noted in the agreement are the many barriers to this goal including DHS limited capacity and high indigent care demands, high managed care penetration rates, and low hospital reimbursements, among others.

Update on Fiscal Outlook

In June 2002, DHS projected an annual funding shortfall of \$709 million in Fiscal Year 2005-06, the year following expiration of the County's 1115 Waiver. At that time, your Board adopted a plan to reform and redesign the County's health system to reduce this funding gap to \$351.9 million. As you can see from the attached schedule, the passage of Measure B, the acceleration of Rancho alternative governance or closure (and related DSH redistribution under current law), and the State/Federal Transition Agreement will further reduce it to \$205.2 million.

Notwithstanding this substantial progress, there is still more work to do. The State's SPCP Waiver must continue to be renewed by the Federal Government on terms favorable to us. We must fully realize the savings goals under Scenario III (four-hospital model) of the Department's Strategic Plan and find ways to close the expected cumulative funding shortfalls that begin in FY 06-07 (see attached schedule). Toward this end, we will continue to work to accomplish DSH flexibility, managed care supplemental payments, and Federal matching of Measure B funds paid to the private sector, as well as explore any other avenues of potential funding. We will also work to address the challenges likely to result from future State and Federal budgets, including potential Medicaid reforms, and accelerating health care inflation.

I will continue to keep you updated on the Department's progress.

TLG:jw

Attachment

cc: Chief Administrative Officer
Executive Office, Board of Supervisor
County Counsel

FISCAL OUTLOOK - 2/10/03

(\$ IN MILLIONS)

	FISCAL YEARS						TOTAL
	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	
Surplus/Deficit as of June 26, 2002		(\$326.6)	(\$549.2)	(\$709.4)			
Scenario III Reductions		120.9	248.2	296.2	n/a	n/a	n/a
Scenario III Other Adjustments/Use of Designation Funds		146.9	79.6	61.3			
Original Fiscal Stabilization Revenue Request to help fund Scenario III (Not Budgetary Shortfall by FY)		(\$58.8)	(\$221.4)	(\$351.9)	(\$387.3) ^(a)	(\$423.7) ^(a)	(\$1,443.1) ^(b)
Forecast Update	\$0.0 ^(b)	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0	\$0.0
Current Surplus/(Shortfall)	\$0.0 ^(b)	(\$58.8)	(\$221.4)	(\$351.9)	(\$387.3)	(\$423.7)	(\$1,443.1)
Additional Funding							
Measure B ^(c)		\$140.0	\$140.0	\$140.0	\$140.0	\$140.0	\$700.0
Acceleration of Rancho Alternative Governance or Closure		58.6					58.6
Current law DSH redistribution if Rancho and High Desert Closed			6.7	6.7	6.9	7.1	27.4
<u>State/Federal Transition Agreement</u>							
SPCP/UPL (SB 1255)	80.0	70.0 ^(d)	50.0	? ^(e)	? ^(e)	? ^(e)	200.0
Outpatient Lawsuit Settlement - Federal Share	50.0	-	-	-	-	-	50.0
Subtotal Additional Funds	\$130.0	\$268.6	\$196.7	\$146.7	\$146.9	\$147.1	\$1,036.0
Annual Surplus/(Shortfall) ^{(e),(f)}	\$130.0	\$209.8	(\$24.7)	(\$205.2)	(\$240.4)	(\$276.6)	(\$407.1)
Cumulative Surplus/(Shortfall) ^{(e),(f)}	\$130.0	\$339.8	\$315.1	\$109.9	(\$130.5)	(\$407.1)	(\$407.1)

Notes:

(a) These amounts are extrapolations from the original 90% Medicaid block grant request used to determine the fiscal stabilization revenues for the June 2002 DHS Strategic Plan, which only extended through FY 05-06.

(b) The current DHS estimated shortfall is in the process of being updated.

(c) Amounts are planning estimates only, subject to refinement and Board approval.

(d) \$20M of the FY 03-04 SPCP-UPL dollars may require DSH flexibility to be retained.

(e) Per State DHS, CMS may "re-base" the Medicaid Upper Payment Limit (**UPL**) beginning FY 05-06. The impact on County DHS of this potential action is estimated to result in reductions of Medicaid revenues from FY 02-03 levels. These estimated reductions totaling **\$374.6M**, are **\$97.6M**, **\$124.9M** and **\$152.1M** for FYs 05-06, 06-07 and 07-08, respectively, and are not reflected in the above. When the UPL is fully implemented, the value could be as high as \$198M. There is also a non-hospital clinic UPL, which the State has yet to compute, that could further reduce County DHS' Medicaid revenues. Further, the full realizability of the Scenario III savings, future State and Federal Budgets, accelerating healthcare inflation, and the President's Medicaid Relief Proposal create significant uncertainty regarding the Department's Fiscal Outlook.

(f) These amounts are potentially improved by managed care supplement and DSH flexibility proposals currently being worked on with the State and Federal governments.